

VZCZCXRO4634
PP RUEHDBU
DE RUEHTA #0410/01 0340218
ZNY CCCCC ZZH
P 030218Z FEB 06
FM AMEMBASSY ALMATY
TO RUEHC/SECSTATE WASHDC PRIORITY 3904
INFO RUEHAK/AMEMBASSY ANKARA 1810
RUEHAH/AMEMBASSY ASHGABAT 6867
RUEHKB/AMEMBASSY BAKU 0616
RUEHBJ/AMEMBASSY BEIJING 1231
RUEHEK/AMEMBASSY BISHKEK 7351
RUEHDBU/AMEMBASSY DUSHANBE 1557
RUEHIL/AMEMBASSY ISLAMABAD 2010
RUEHBUL/AMEMBASSY KABUL 0126
RUEHKV/AMEMBASSY KIEV 2422
RUEHMO/AMEMBASSY MOSCOW 1127
RUEHNE/AMEMBASSY NEW DELHI 0292
RUEHNT/AMEMBASSY TASHKENT 7322
RUEHSI/AMEMBASSY TBILISI 2168
RUEAIIA/CIA WASHDC
RUEBAAA/DEPT OF ENERGY WASHDC

C O N F I D E N T I A L SECTION 01 OF 03 ALMATY 000410

SIPDIS

SIPDIS

DEPT FOR EB/ESC; EUR/SNEC (MANN); EUR/CACEN (MUDGE, O'MARA)

E.O. 12958: DECL: 02/01/2015

TAGS: [ENRG](#) [EPET](#) [KZ](#) [CH](#)

SUBJECT: KAZAKHSTAN-CHINA GAS PIPELINE PROJECT: STATUS
UPDATE

REF: ALMATY 323

Classified By: POEC Chief Deborah Mennuti for reasons 1.4(B) and (D)

1. (C) Summary: The state-owned Kazakhstani and Chinese oil and gas companies recently completed a "pre-feasibility study" for the construction of a 30 billion cubic meter (bcm) gas pipeline from Central Asia to China. The study outlines three proposed pipeline routes across Kazakhstan, the economic and technical merits of which will be analyzed in the next-stage "feasibility study," targeted for completion by year-end 2006. While Kazakhstan's "big three" oil fields -- Karachaganak, Tengiz, and Kashagan -- are the logical source for associated gas to fill the pipeline, discussions to secure guaranteed volumes of gas from those fields for the pipeline are in their infancy. A gas pipeline to China would give Kazakhstan needed relief from its current dependence for gas exports on the Gazprom monopoly. However, despite its clear advantages, the project's complexity and expense, along with Kazakhstani fears of Chinese monopsonistic power, render the project's future uncertain. End Summary.

Progress: From "Pre-Feasibility" to "Feasibility" Study

2. (C) KazMunaiGas (KMG) subsidiary "Kazakh Institute of Oil and Gas" (KIOG) and the Chinese Petroleum Pipeline Engineering Institute (a CNPC subsidiary) recently completed a joint "pre-feasibility study" on a potential Kazakhstan-China gas pipeline. According to Sabr Yessimbekov, Executive Director of KMG's Oil and Gas Transportation Division, the pre-feasibility study (a) established China's medium-term need for at least 30 bcm of Central Asian gas, and (b) outlined three potential routes for a gas pipeline across Kazakhstan. KMG is now contributing economic and technical analysis to the project's "feasibility study," due to be completed by year-end 2006. Based on the findings of the feasibility study, Yessimbekov explained, a route would be chosen and engineering work begun.

3. (C) While Yessimbekov's office is studying issues of tariffs and take-off prices, KIOG is providing technical and engineering analysis. The Institute's Director, Dr. Serik Burkitbayev, told Econoff that a combination of the pipeline's length (3000 km in Kazakhstan alone, according to one variation), and the high volume of gas (30 bcm) required to make the project economically viable, made the project a "true engineering challenge." Pressures of up to 140 bars would have to be maintained in a large-diameter pipeline, necessitating the "newest metals and the best technologies." Russian technology "wouldn't be good enough," he said, adding that he hoped that Western firms would participate in the project.

Choosing Between Three Proposed Routes

4. (SBU) Three principal routes are being considered for the pipeline: (a) a "Northern" route, which would enter Kazakhstan from Russia at Petropavlosk, and continue through Astana, Karaganda and Atasu, where it would parallel the recently-completed second leg of the Kazakhstani-Chinese oil pipeline (reftel) to the Chinese city of Alashankou; (b) a "Central" route, from Makat (a pumping station on the Central Asian Gas Pipeline, near Atyrau) through Kenkijak, Chelkar, Karakojyn, and Balkash, and on to Alashankou; and (c) a "Southern" route, which would run from Makat to Chelkar, then Southeast through Aralsk, Kyzylorda, Taraz, and Almaty, and on to the Chinese border at either Khorgos or Alashankou.

5. (C) Yessimbekov indicated that the Chinese were also interested in a variation of the Southern route. Under this proposal, the existing Gazli (Uzbekistan) - Shymkent - Almaty

ALMATY 00000410 002 OF 003

gas pipeline would be repaired, expanded, and extended from Almaty to the Chinese border. However, Yessimbekov said, the Chinese did not know it yet but President Nazarbayev had "just sent the signal" to exclude this option from consideration. "We don't want Turkmenistan's and Uzbekistan's participation in this project," he explained. Burkitbayev echoed Yessimbekov's distrust of Uzbek involvement, casting doubt on Uzbekistan's ability to supply gas for export. Due to subsidized gas prices, he said, "the Uzbeks use 95% of their gas domestically. And they have shortages every winter."

16. (C) Burkitbayev and Yessimbekov outlined advantages and disadvantages of all three routes for both the Kazakhstanis and the Chinese. The Chinese favored the Central route because it bypassed major Kazakhstani population centers, thus delivering 100% of the gas for China. The Southern route was ideal for Kazakhstan: not only would it help solve the problem of bringing Caspian gas to market, it would also require the least investment, by utilizing existing gas lines. Furthermore, it would bring gas to the Almaty's gas-starved South, thus freeing that region from energy dependency on Uzbekistan. Burkitbayev explained that in a worst-case scenario -- in which the Chinese, for whatever reason, abruptly refused to take delivery of the gas -- the Kazakhstanis would be able to find a use for "30-50%" of the gas along the Southern route. On the other hand, the Chinese were unhappy with the fact that the Kazakhstanis would "lift" a significant amount of gas from a Southern pipeline, leaving less for delivery to the border.

17. (C) The Northern pipeline had the advantage of passing through Astana and Karaganda, where additional gas could be used to support population and industrial growth. Swaps into this line could work to Kazakhstan's advantage, with Kazakhstani gas delivered to Russia in Kazakhstan's gas-rich West, in return for Russian gas delivered into the Northern pipeline. However, the Northern route would leave the project dependent on Gazprom -- the very problem the Chinese gas pipeline was meant to alleviate.

Where Will the Gas Come From?

18. (C) Haunting all of these discussions, Yessimbekov admitted, was the question of where the Kazakhstani gas to fill a Central or Southern pipeline would come from. In geological terms, the answer is evident: over 70% of Kazakhstan's proven gas reserves lie in just three fields: Karachaganak, Tengiz, and Kashagan. Production of this "associated gas" will grow dramatically in the near-term as a consequence of planned increases in crude production at all three fields. Increased gas production from these fields, in turn, comprises the bulk of the GOK's forecasted short-term growth in gas production and export.

19. (C) However, while either the Central or Southern pipeline would be well-placed to tap gas from these fields, negotiations to secure guaranteed gas supplies for the pipeline were, in Yessimbekov's words, "barely getting started." Complicating factors include the producing companies' desire to re-inject high volumes of gas in (irdurJto"maqntaIn nil,reserwoir rrucwtre,!hm g0unePkb!Beid)riQ*y1QollT\$esQxsQuy1)N&gaSkoc

ALMATY 00000410 003 OF 003

of the Ukrainian-Russian gas dispute (Burkitbayev, for example, told Econoff that his Institute had just been instructed to "begin looking into" the project), the pipeline to China is the only gas transportation project underway which lessens Kazakhstan's dependence on Gazprom. However, growing Chinese involvement also comes with a price. Burkitbayev told Econoff (and Yessimbekov confirmed) that the Chinese had predicated their participation in the pipeline project on being granted offshore oil and gas blocks -- ostensibly to secure their own gas reserves with which to fill the pipeline.

11. (C) The GOK is also wary of increasing its dependence on a monopsonistic buyer of oil and gas. When Econoff asked Yessimbekov if he thought the project would ever be realized, he hesitated before answering. "Two weeks ago, I might have said 'yes'," he replied. However, he said, the Kazakhstani Embassy in Beijing had just written an "extremely persuasive" report warning of the dangers of over-dependence on China as a buyer of Kazakhstani oil and gas. As a consequence of the report, he said, "enthusiasm for the gas pipeline project has cooled."

ORDWAY